Insurance Test Practice

New Jersey Insurance Practice Test

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1. Which of the following statements about the interest rate guaranteed in a fixed annuity is CORRECT?

A) The guaranteed rate is the only rate ever credited
✓ B) The insurer may credit a higher current rate but guarantees a minimum rate for the life of the contract
C) Guaranteed rates only apply during the surrender charge period
D) The guaranteed rate resets each year based on Treasury yields

Explanation: Fixed annuities guarantee a minimum interest rate for the life of the contract. The insurer may credit a higher current (declared) rate, but the minimum is the floor. Historically, minimum guarantees have ranged from 1% to 3.5% depending on when the contract was issued. The current credited rate can be reset periodically but cannot fall below the contractual minimum.

2. A mutual insurance company is owned by:

A) The state insurance department
B) Stockholders who receive dividends
C) Federal banking regulators
✓ D) Policyholders who may receive dividends from surplus

Explanation: A mutual insurance company is owned by its policyholders. Profits (surplus) may be returned to policyholders as dividends, which are considered a non-taxable return of excess premium. Mutual companies have no stockholders.

3. All variable product sales must be suitable for the customer. Suitability is determined by evaluating all of the following EXCEPT:

A) The customer's financial situation and needs
✓ B) The customer's political affiliations
C) The customer's tax status
D) The customer's investment objectives and risk tolerance

Explanation: FINRA suitability rules require that any recommendation of a variable product be based on a thorough evaluation of the customer's financial situation, investment objectives, risk tolerance, tax status, time horizon, liquidity needs, and existing holdings. Personal characteristics like political affiliation are irrelevant to suitability.

4. A producer who finds out that an insurer they are appointed with has become financially impaired should:

A) Immediately place new business with that insurer to help it recover financially
B) Continue placing business until DOBI formally revokes the insurer's license
✓ C) Stop placing new business with that insurer and advise existing policyholders to consider their options
D) Take no action until a client experiences a claim denial

Explanation: A producer has an ethical and fiduciary duty to their clients. Upon learning of an insurer's financial impairment, the producer should stop recommending that company for new business and should proactively inform affected clients of the situation so they can make informed decisions about their coverage. Continued placement with a financially impaired insurer could harm clients and expose the producer to liability.

5. To sell Variable Universal Life insurance, an agent must hold which of the following licenses?

A) Accident and Health agent license
✔ B) Both a Life-Only agent license and a FINRA Series 6 or 7 securities license
C) FINRA Series 6 or 7 license
D) Life-Only agent license

Explanation: Variable products are considered both insurance and securities. Therefore, the agent needs both a state life insurance license and a federal securities license (Series 6 or 7).

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6. The 'comparison' requirement in NJ replacement regulations means:

A) The insurer must compare its rates to all competitors before issuing a replacement policy
B) DOBI compares the replacement to the original policy to verify its suitability
✔ C) The producer must provide information comparing the existing policy and proposed replacement to help the consumer make an informed decision
D) The producer must provide a written comparison of three competing policies

Explanation: NJ replacement regulations require the producer to prepare and provide to the applicant a comparison of the existing policy and the proposed replacement — including policy values, costs, benefits, and any potential losses or gains from the replacement. This ensures the consumer has sufficient information to evaluate whether the replacement is in their interest.

7. Long-term care insurance benefit triggers typically include:

A) Any hospitalization lasting more than 5 days
B) Loss of income due to disability or injury
C) Any diagnosis of a chronic illness by a physician
✔ D) Inability to perform at least 2 of 6 Activities of Daily Living (ADLs) or severe cognitive impairment

Explanation: LTC insurance benefits are triggered when the insured cannot perform at least 2 of 6 Activities of Daily Living (ADLs): bathing, dressing, eating, continence, toileting, and transferring. Severe cognitive impairment (such as Alzheimer's) is also a trigger. Both triggers must be certified by a licensed healthcare practitioner.

8. Which of the following is an advantage of term life insurance?

A) It provides lifelong coverage.
B) The premium never increases.
✔ C) It has the lowest initial premium for a given face amount.
D) It builds cash value.

Explanation: The primary advantage of term life insurance is its affordability. It provides the largest amount of death benefit for the lowest initial premium, making it an accessible option for temporary, high-need situations like protecting a young family.

9. Arthur is 66 years old, retired, and enrolled in Medicare Parts A and B. He has group health coverage through his spouse's active employment at a large company (150 employees). If Arthur incurs a medical bill, how is the claim coordinated?

A) Medicare is primary; the group plan is secondary
✓ B) The group plan is primary; Medicare is secondary
C) Medicare pays 100% and the group plan pays nothing
D) The plans split the cost evenly

Explanation: When an individual age 65 or older is covered by an employer group health plan through active employment (either their own or their spouse's) at an employer with 20 or more employees, the group health plan is the primary payer and Medicare is the secondary payer.

10. To prevent a universal life policy from becoming a MEC (Modified Endowment Contract):

A) The policyowner must keep cash value below the net amount at risk
B) No single premium payment can exceed the face amount
C) The policyowner must take a policy loan each year to reduce the cash value below MEC limits
✓ D) Total premiums paid must not exceed the 7-pay limit — the amount needed to fully fund the policy in 7 level annual payments

Explanation: The IRS 7-pay test determines MEC status. If a policy is funded faster than a hypothetical 7-year level premium payment schedule allows, it becomes a MEC. Policyowners who want to maximize cash value while maintaining life insurance tax advantages (tax-free loans and withdrawals up to basis) must be careful not to over-fund beyond 7-pay limits.

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11. The NJ Small Employer Health Benefits (SEHB) Program protects small businesses by:

A) Subsidizing premiums for employees earning below the poverty level
B) Exempting small employers from all ACA requirements
C) Providing free health insurance to employers with fewer than 10 employees
✓ D) Requiring insurers to offer health coverage to small employers on a guaranteed-issue basis with community rating

Explanation: The NJ SEHB Program (applying to employers with 2-50 employees) requires participating insurers to offer health coverage to small employers on a guaranteed-issue basis. It also restricts rating practices, typically requiring modified community rating to prevent discrimination against sicker employee groups.

12. Variable health benefit products require the selling producer to hold:

A) A NJ property and casualty license
B) Only a state health insurance license
✓ C) Both a state health insurance license and appropriate FINRA securities registrations
D) Only a FINRA securities license

Explanation: Variable health benefit products are classified as both insurance and securities products because their benefits are linked to investment performance. As with variable annuities and variable life, producers must hold both a state insurance license and the required FINRA securities registrations (e.g., Series 6 or 7).

13. What is 'respite care' in the context of an LTC policy?

- ✔ A) Temporary care to provide a break for the primary caregiver.
- B) Care provided by a family member.
- C) Care provided in a hospital.
- D) Care provided at the end of life.

Explanation: Respite care is a common benefit in LTC policies. It pays for a temporary stay in a nursing facility or for a home health aide to come in, allowing the regular, often unpaid, family caregiver to get a much-needed break.

14. The annual HSA contribution limit is set by the IRS and includes both employer and employee contributions. Individuals age 55 and older can make additional 'catch-up' contributions of:

- A) $500 per year
- B) $1,500 per year
- ✔ C) $1,000 per year
- D) $2,000 per year

Explanation: Individuals who are age 55 or older by the end of the tax year are permitted to make an additional catch-up contribution of $1,000 per year above the standard annual limit. This catch-up amount is set by law and is not indexed for inflation.

15. An investor has an Equity Indexed Annuity tied to the S&P 500. The index rises by 15% during the year. The policy has a participation rate of 80% and a cap rate of 10%. What index interest rate will be credited to the investor's annuity?

- A) 15%
- B) 12%
- ✔ C) 10%
- D) 8%

Explanation: The participation rate would yield 12% (80% of 15%). However, because the policy has a cap rate of 10%, the maximum interest that can be credited is limited to the cap of 10%.

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16. When replacing existing life insurance in NJ, the producer must leave with the applicant:

- A) A statement from DOBI approving the replacement
- ✔ B) A signed copy of the replacement notice (Form A) and a comparison document (Form B) describing the replacement transaction
- C) A copy of the producer's license
- D) Only the new policy's summary page

Explanation: In NJ, when a life insurance replacement transaction occurs, the producer must: (1) present and have the applicant sign a Notice Regarding Replacement (Form A), which discloses the replacement and advises the applicant of potential disadvantages; (2) provide Form B, a comparison statement. The producer gives the applicant a signed copy of Form A and keeps a copy. These forms must be submitted to the replacing insurer, which notifies the existing insurer.

17. When a client surrenders an existing annuity to purchase a new one recommended by their producer, the producer's duty includes:

A) Guaranteeing the new annuity will perform better than the old one
B) Only disclosing the surrender charges on the old annuity
C) Only ensuring the paperwork is completed correctly
✔ D) Evaluating whether the replacement is suitable and in the client's best interest, disclosing all material differences, and completing NJ replacement requirements

Explanation: Annuity replacement carries significant fiduciary duties. The producer must: assess suitability of the new product, disclose any surrender charges or penalties on the existing contract, explain how the new contract compares, complete NJ replacement notices, and document that the recommendation is in the client's best interest. Recommending replacement solely to generate new commissions is a serious violation.

18. A Risk Retention Group (RRG) is:

✔ A) A liability insurance company owned by its members to insure similar risks
B) A reinsurance pool for admitted insurers
C) A self-funded health plan for large employers
D) A state-created fund that retains premium until claims are paid

Explanation: A Risk Retention Group (RRG) is a liability insurance company formed under the federal Liability Risk Retention Act, owned by its member-insureds, and formed to insure risks shared by members of a similar industry or trade group.

19. 'Separate account' assets in variable life insurance are:

✔ A) Legally segregated from the insurer's general account and protected from the insurer's creditors
B) Blended with the insurer's general account for unified investment management
C) Accessible only after the insurer's general account obligations are satisfied
D) Managed by a federally regulated bank on behalf of the insurer

Explanation: The separate account in a variable life or variable annuity product is legally segregated from the insurer's general account assets. This segregation protects policyholders' subaccount investments from the insurer's creditors in the event of insolvency. Separate account assets are NOT available to the insurer's general creditors.

20. If an insured's age is found to be understated on a life insurance application, what will the insurer do at the time of claim?

A) Pay the full claim but require the beneficiary to pay back premiums
B) Void the policy due to misrepresentation
C) Pay the full claim without adjustment
✔ D) Pay a reduced death benefit

Explanation: Under the Misstatement of Age provision, the insurer will adjust the death benefit to the amount the premium would have purchased had the correct age been stated. They will not void the policy after the contestability period.

21. Under the ACA for plan years beginning on or after January 1, 2014, annual and lifetime dollar limits on:

A) All benefits are prohibited
B) All limits were grandfathered and remain in effect
C) Only inpatient hospital benefits are prohibited
✔ D) Essential health benefits are prohibited; lifetime limits on non-essential benefits may still apply

Explanation: The ACA prohibits annual and lifetime dollar limits on essential health benefits (EHBs) in non-grandfathered plans. Insurers cannot cap the annual or lifetime amount they will pay for EHBs. However, annual and lifetime limits may still be applied to benefits that are not EHBs.

22. In New Jersey, rebating is defined as:

A) Misrepresenting the benefits of a policy to induce replacement
✔ B) Returning a portion of the premium to the insured as an incentive to purchase
C) Selling insurance without a valid appointment
D) Failing to remit collected premiums to the insurer

Explanation: Rebating in New Jersey refers to the illegal practice of giving or offering a policyholder any part of the commission, premium, or other valuable consideration as an inducement to purchase insurance. It is prohibited under NJSA 17B:24.

23. Universal life insurance is distinguished from whole life by its:

A) Guaranteed minimum cash value and fixed premiums
✔ B) Flexible premium payments and adjustable death benefit
C) Requirement for FINRA securities registration to sell
D) Higher cost and shorter policy term

Explanation: Universal Life (UL) insurance offers premium flexibility (the policyowner can pay more or less than a target premium within limits) and an adjustable death benefit (can be increased or decreased subject to insurability requirements). The policy has a minimum premium that must be paid to keep it in force.

24. A 'hospital confinement indemnity' policy pays:

✔ A) A fixed daily benefit for each day the insured is confined in a hospital, regardless of actual charges
B) Only the difference between hospital charges and what the primary insurer pays
C) Hospital bills only for catastrophic illnesses
D) A percentage of hospital charges up to a daily maximum

Explanation: Hospital confinement indemnity policies pay a fixed daily benefit (e.g., $200/day) for each day the insured is confined in a hospital, regardless of the actual hospital charges. These benefits are paid directly to the insured (not to the hospital) and can supplement other health coverage for expenses not covered by primary insurance.

25. Group life insurance usually requires evidence of insurability for employees who:

A) Have had any health conditions in the past 5 years
B) Work part-time fewer than 20 hours per week
C) Are over age 55
✔ D) Enroll late (after the initial enrollment period) without a qualifying life event

Explanation: In group life insurance, late enrollees (those who did not enroll during the initial or open enrollment period without a qualifying life event) are typically required to provide evidence of insurability (a medical statement or exam). This requirement prevents adverse selection by people who only seek coverage when they know they need it.

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26. Under New Jersey law, a producer has a duty to disclose to a client all of the following EXCEPT:

A) Any conflicts of interest that may affect the recommendation
B) Their licensee status and the insurer they represent
C) Material facts about the policy
✔ D) Their commission amount on every policy sold

Explanation: New Jersey producers are required to disclose material facts and conflicts of interest, but there is no general requirement to disclose the exact commission amount on every policy sold unless specifically required by a particular regulatory context (e.g., certain annuity transactions).

27. Non-qualified annuity withdrawals are taxed using the LIFO method, which means:

A) All withdrawals from non-qualified annuities are always tax-free
✔ B) The last money in (earnings/gains) is deemed to come out first and is taxable
C) Withdrawals are taxed as capital gains
D) The first dollars out are tax-free until the cost basis is recovered

Explanation: Non-qualified deferred annuities follow LIFO (Last In, First Out) tax treatment. Earnings (gains) are deemed to be withdrawn first and are taxed as ordinary income. The cost basis (after-tax premiums paid) is recovered last and received tax-free. This contrasts with qualified annuities where all withdrawals are fully taxable.

28. Dividends received from a participating life insurance policy are:

A) Taxable as ordinary income.
B) Tax-deductible for the policyowner.
C) Taxable as capital gains.
✔ D) Generally considered a tax-free return of premium.

Explanation: Policy dividends are not guaranteed and are considered a return of an overpayment of premium. As such, they are not taxable income to the policyowner. However, if dividends are left to accumulate at interest, the interest earned is taxable.

29. A New Jersey producer discovers that a client's application contains a material misrepresentation. What is the producer's ethical obligation?

- ✔ A) Correct the misrepresentation and inform the client and insurer
- B) Deny coverage unilaterally on the insurer's behalf
- C) Refund the client's premium immediately
- D) Submit the application as-is to avoid delay

Explanation: A producer has an ethical and legal duty to ensure that applications are accurate. Knowingly submitting a materially false application constitutes fraud in New Jersey. The producer must inform the client of the discrepancy and submit accurate information to the insurer.

30. In insurance, the proximate cause of a loss refers to:

- A) The most expensive cause of a loss
- ✔ B) The dominant or effective cause that sets a chain of events in motion resulting in a loss
- C) Any event that contributes to a loss
- D) The last event in a chain of events leading to a loss

Explanation: Proximate cause is the dominant, effective, or direct cause that sets in motion an unbroken chain of events leading to a loss. It is used to determine whether a loss is covered under a policy.

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31. Under NJ's Insurance Fraud Prevention Act, civil penalties for a single violation can be as high as:

- A) $25,000
- B) $500
- C) $1,000
- ✔ D) $5,000 (plus treble damages for certain violations)

Explanation: The NJ Insurance Fraud Prevention Act provides for civil penalties of up to $5,000 for a first violation and higher amounts for subsequent violations, plus possible treble damages (three times the amount fraudulently obtained) and attorney fees. Criminal penalties may also apply. The law targets insurers, producers, and policyholders who commit insurance fraud.

32. A purchasing group under the federal Liability Risk Retention Act:

- A) Is the same as a risk retention group
- ✔ B) Enables a group to purchase liability insurance on behalf of members from admitted or risk retention group insurers
- C) Purchases property insurance for municipalities
- D) Provides coverage only for professional liability

Explanation: A Purchasing Group is a group formed under the federal Liability Risk Retention Act to purchase liability insurance on behalf of its members from an insurer that is either admitted in a member's state or a risk retention group. Purchasing groups have more regulatory freedom to operate across state lines.

33. A Guaranteed Lifetime Withdrawal Benefit (GLWB) rider on a deferred annuity provides that the owner can:

A) Annuitize the contract at a future date.
B) Receive a guaranteed minimum interest rate.
C) Withdraw the entire contract value at any time without a charge.
✔ D) Withdraw a specified percentage of the contract value each year for life, even if the actual account value drops to zero.

Explanation: A GLWB rider is a popular feature that offers a form of lifetime income without forcing the owner to annuitize the contract. It guarantees that the owner can take systematic withdrawals for life, providing income security while maintaining access to the underlying account value.

34. Life insurance proceeds paid directly to a named beneficiary (not the insured's estate):

✔ A) Generally bypass probate and are paid directly to the beneficiary
B) Are always subject to income tax for the beneficiary
C) Are subject to federal estate tax in all cases
D) Must be held in trust for minor beneficiaries by law

Explanation: Life insurance proceeds paid to a named beneficiary generally bypass the probate process entirely and are paid directly to the beneficiary. This is a significant advantage of naming specific beneficiaries rather than using the estate as beneficiary. Estate taxes may still apply depending on who owns the policy.

35. A contract requires that both parties bring something of value to the exchange. This is known as:

A) Competent Parties
✔ B) Consideration
C) Agreement
D) Legal Purpose

Explanation: Consideration is the value that each party gives in the contractual agreement. The insured's consideration is the premium paid and the statements on the application; the insurer's is the promise to pay claims.

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36. A policyowner named his wife as the primary beneficiary and his son as the contingent beneficiary. The wife dies several years before the insured. When the insured dies, who receives the death benefit?

A) The wife's estate
B) The insured's estate
✔ C) The son
D) The proceeds are split between the son and the insured's estate.

Explanation: The contingent beneficiary's role is to receive the proceeds if the primary beneficiary is no longer living when the insured dies. Since the wife predeceased the insured, the son, as the contingent beneficiary, receives the full death benefit.

37. Which party to an annuity contract is the person whose life expectancy is used to calculate the income payments?

A) The insurer
✔ B) The annuitant
C) The beneficiary
D) The owner

Explanation: The annuitant is the individual upon whose life the annuity payments are based. The owner and the annuitant are often the same person, but not always.

38. When does legal delivery of an insurance policy occur?

A) When the insurer mails the policy to the agent
B) When the agent receives the policy from the insurer
C) When the insured signs the policy acceptance form
✔ D) When the agent delivers the policy to the insured and collects any premium due

Explanation: Legal delivery is not just the physical delivery of the policy. It is a constructive process that occurs when the policy is delivered to the applicant by the producer and the first premium is paid, assuming there has been no change in the applicant's health.

39. A 'Lloyd's of London' syndicate functions as:

A) A surplus lines insurer offering standardized policies
B) A government-backed reinsurance facility
C) A stock insurance company with publicly traded shares
✔ D) A marketplace where individual underwriters and syndicates accept portions of risks brought by brokers

Explanation: Lloyd's of London is not an insurance company — it's a marketplace where syndicates (groups of underwriters and investors) accept portions of unique or large risks. Brokers bring risks to Lloyd's syndicates, which can each take a percentage of the risk. Lloyd's is particularly known for insuring unusual, large, or hard-to-place risks. In NJ, Lloyd's underwriters are non-admitted carriers accessible through surplus lines brokers.

40. A fraternal benefit society differs from a stock or mutual insurer because it:

A) Only provides group life insurance to employers
B) Is regulated by the federal government, not state agencies
✔ C) Is nonprofit and sells insurance only to its own members through a lodge system
D) Sells coverage to the general public without any membership requirement

Explanation: A fraternal benefit society is a nonprofit organization with a lodge or ritualistic structure that provides insurance and social benefits only to its members. Membership is usually based on a common bond such as religion, ethnicity, or profession.

41. The process of evaluating a risk to determine if it is acceptable to an insurer is called:

A) Claims adjusting
B) Reinsurance
✔ C) Underwriting
D) Marketing

Explanation: Underwriting is the process of risk selection, classification, and pricing. Underwriters for the insurance company decide whether to accept or reject applications for insurance.

42. In New Jersey, how long is the suicide exclusion period in a standard individual life insurance policy?

A) 3 years from the policy date
B) 1 year from the policy date
✔ C) 2 years from the policy date
D) There is no suicide exclusion in NJ

Explanation: New Jersey allows life insurers to exclude suicide as a covered cause of death for the first 2 years from the policy date. After 2 years, the insurer must pay the death benefit even if the cause of death is suicide.

43. When an applicant pays the first premium at the time of application, the agent typically gives them a:

A) Policy summary
B) Binder
✔ C) Conditional receipt
D) Statement of Good Health

Explanation: A conditional receipt is given when the premium is paid with the application. It provides that coverage will become effective as of the date of the application or medical exam, whichever is later, provided the applicant is found to be insurable as a standard risk.

44. Robert names his wife, Linda, as the primary beneficiary of his life insurance policy and his son, Tim, as the contingent beneficiary. If Robert and Linda are in a fatal car accident and Linda dies two hours before Robert, who receives the death benefit?

A) Linda's estate
B) Robert's estate
✔ C) Tim
D) Split equally between Linda's estate and Tim

Explanation: Because Linda (the primary beneficiary) predeceased the insured (Robert), the contingent beneficiary (Tim) is entitled to receive the death benefit.

45. The term 'fiduciary' refers to:

✔ A) A person in a position of special trust and confidence
B) The person who receives policy benefits
C) An insurance company's main office
D) A legal entity

Explanation: A fiduciary is a person or organization that holds a position of financial trust and confidence when handling the affairs or funds of another. Insurance producers have a fiduciary duty to their clients and the insurer.

46. The ACA requires applicable large employers (ALEs) — those with 50 or more full-time employees — to:

A) Cover all employees including part-time employees who work at least 10 hours per week
B) Provide health insurance to all employees within 30 days of hire
✓ C) Offer minimum essential coverage to full-time employees and their dependents or potentially owe an employer shared responsibility payment
D) Reimburse employees for individual marketplace coverage purchases

Explanation: Under the ACA's employer shared responsibility provision (employer mandate), ALEs with 50+ full-time employees must offer minimum essential coverage (MEC) that is affordable and meets minimum value to full-time employees (and their dependents) or potentially owe a penalty if any full-time employee receives a premium tax credit through the marketplace.

47. What is the waiting period before Social Security Disability Insurance (SSDI) benefits begin?

A) 12 months
B) 6 months
✓ C) 5 months
D) 3 months

Explanation: There is a mandatory 5-month waiting period before SSDI benefits begin. Benefits are first payable for the sixth full month after the onset of the disability. This waiting period serves as a type of elimination period similar to private disability insurance.

48. The cash value in a permanent life insurance policy belongs to:

A) The state guaranty fund until a claim is paid
✓ B) The policyowner
C) The beneficiary
D) The insurer, until the insured dies

Explanation: The cash value (also called the policy reserve) in a permanent life insurance policy belongs to the policyowner. The policyowner can access it through a policy loan, surrender the policy for the cash value, or use it to fund policy provisions such as the paid-up option.

49. What is the minimum age to obtain a resident insurance producer license in New Jersey?

A) 21 years old
B) 16 years old
C) 17 years old
✓ D) 18 years old

Explanation: New Jersey requires that a resident insurance producer applicant be at least 18 years of age. This is a standard requirement under NJ licensing law administered by the DOBI.

50. Under NJ insurance law, an 'admitted insurer' must:

✔ A) Be licensed by DOBI to transact insurance in New Jersey
B) Have been in business for at least 25 years
C) Maintain its headquarters in New Jersey
D) Have at least $1 billion in assets

Explanation: An admitted insurer in New Jersey is one that has obtained a Certificate of Authority from DOBI, authorizing it to transact insurance business in the state. Admitted insurers are subject to NJ rate and form regulation and their policyholders are protected by the NJ Guaranty Association.